ST 98-38
Tax Type: SALES TAX
Issue: Responsible Corp. Officer - Failure to File or Pay Tax
Timeliness of Protest (60-Day Limitation)

STATE OF ILLINOIS
DEPARTMENT OF REVENUE
OFFICE OF ADMINISTRATIVE HEARINGS
CHICAGO, ILLINOIS

THE DEPARTMENT OF REVENUE OF THE STATE OF ILLINOIS	**No. 97-ST-0000** **Reg. No. 0000-0000** **NPL No. 0000**
v.	
"DONALD DUCK", Responsible Officer Of "Daisy Chain, Inc.,	**Charles E. McClellan** **Administrative Law Judge**
Taxpayer	

RECOMMENDATION FOR DECISION

Appearances:

John D. Alshuler for the Illinois Department of Revenue. Sheldon A. Brenner, of Brenner & "Duck", Ltd., for the respondent.

Synopsis:

This matter came on for evidentiary hearing on October 28, 1998, following the filing of a timely protest to a Notice of Penalty Liability ("NPL") issued by the Department of Revenue ("Department") on June 2, 1993, to "Donald D. Duck" ("Duck "). The NPL, in the amount of $33,411.81, was issued to "Duck" as a responsible officer of "Daisy Chain, Inc.", a retailer located at "Anystreet", "Anytown", Illinois. At a status conference on December 1, 1998, both parties waived their opportunity to file post hearing briefs and agreed to have this case decided on the basis of the testimony transcribed at the hearing and the documents of record.

There are two issues to be addressed: The first issue is whether "Duck" was a responsible officer or employee of the corporation that incurred the underlying tax liability. If the answer to the first issue is that the NPL was issued properly, the second issue is whether "Duck" is liable, as a responsible person, for the penalty

assessed him under section 13 ½ of the Retailers' Occupation Tax Act ("ROTA") Ill. Rev. Stat. 1991, ch. 120, ¶ 452½.[1].

Following the submission of all evidence and a review of the record, I recommend that the Department's NPL be made final.

Findings of Fact:

1. NPL 0000 was issued to "Donald D. Duck" as a responsible officer of "Daisy Chain, Inc." ("Chain") on June x, 19xx. Dept. Ex. No. 1.

2. The registration number of "Chain", as shown on the NPL is 0000-0000. *Id.*

3. The Sales and Use Tax Returns (Form ST-1) for the months of August 1990 through December 1990 were filed for a taxpayer designated as "Daisy Chain, Inc.", "Anystreet", "Anytown" filing under Illinois Business Tax ("IBT") number 0000-0000. Dept. Ex. No. 2, Taxpayer[2] Exs. No.1, 2, 3, 4, 5.

4. "Duck", whose address is 111 East "Quack" Street, "Duckville", Illinois, served as president of "Chain" at all relevant times starting with its incorporation. Tr. pp. 14, 23.

5. The organizers of "Chain" began start up activities in 1987. Tr. p. 21.

6. There were three cash investors and one "sweat-equity" investor. Tr. p. 22.

7. "Mickey Mouse", was the sweat-equity investor and the corporate secretary. Tr. pp. 22, 23.

8. "Duck" was the corporation's president. Tr. pp. 23, 24.

9. "Duck" had a $70,000 cash equity investment in "Chain" which was the same as the other two monetary investors. Tr. p. 27.

10. "Duck" also guaranteed debts of "Chain". *Id.*, Tr. p. 28.

11. "Chain" retained outside accountants to see that the business was properly run and had a qualified bookkeeper employee, "Penelope Pennypacker", whose name appeared on some of the tax returns. Tr. pp. 31, 32.

12. "Duck" signed some of the sales tax returns filed for the business. Tr. p. 24.

13. "Duck" never received a salary or money of any sort from "Chain". Tr. p. 32.

14. "Chain" opened for business about June 1988. Tr. p. 32.

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[1] Ill. Rev. Stat. 1991, ch. 120, ¶ 452½, was repealed effective January 1, 1994. It was replaced by § 3-7 of the Uniform Penalty and Interest Act, 35 ILCS 735/7. "Duck's" liability in this case is determined under § 13½ of the ROTA, the law in effect during 1990 and 1991 when the tax was incurred. Musa Sweis v. Department of Revenue, 269 Ill. App. 3d 1, 645 N.E. 2d 972 (1st Dist. 1995).

[2] Each of taxpayer's exhibits 1 through 5 is identified in the record as "Respondent Exhibit" rather than "Taxpayer Exhibit".

15. The general manager at that time was "Myron Mouse", Mickey Mouse's" brother. Tr. p. 33.

16. "Myron Mouse" was discharged during the fall of the first year of operation. Tr. pp. 33, 34.

17. "Mickey Mouse" took over as general manager until "Huey Duck" was recruited four to six weeks later. Tr. p. 34.

18. "Huey Duck" was discharged after six months because he did not do a good job. Tr. p. 35.

19. "Goofy", an employee, was then given the general manager position. *Id*.

20. In the fall of 1990, "Duck" began getting calls because creditors were not being paid. Tr. p. 37.

21. In the fall of 1990, "Duck" owned 50% of the corporation and Mr. "Pluto" and Mr. "Mouse" each owned 25%. Tr. p. 52.

22. "Duck" had check signing authority. Tr. p. 38.

23. "Duck" signed sales tax returns and checks to pay the taxes during the fall of 1990. *Id*., Dept. Ex. No. 2.

24. Other persons had authority to sign checks to remit sales taxes to the state. Tr. p. 38.

25. "Duck" relied on the fact that "Chain" had a trained in-house bookkeeper, had retained a certified public accounting firm and had the canceled checks and bank statements sent to the accountant for control. Tr. pp. 41, 42.

26. "Duck" did not receive regular reports from the accountants. Tr. p. 50.

27. In the fall of 1990, when "Duck" learned that "Chain" was having financial difficulties he examined the books and records, spoke to the accountants and spoke to the manager. Tr. p. 54.

28. Once "Duck" became aware of the fact that the business was failing, he began receiving verbal financial reports from management. Tr. p. 57.

Conclusions of Law:

The first issue is whether the NPL was addressed to "Duck" as a responsible officer of the corporation that incurred the underlying tax liability. "Duck" testified extensively about whether the sales which ultimately resulted in the liability assessed in this case were made by a corporation by the name of "Daisy Chain, Inc." or by a second corporation named "Daisy Chain, Ltd." "Duck" testified that the business was originally incorporated as an Illinois corporation by the name of "Daisy Chain" Ltd. Tr. p. 20. He stated that the shareholders wanted to make a Subchapter S election under the Internal Revenue Code for federal income tax purposes, but that the election period expired before the election was made. *Id*. He testified that "Daisy Chain"

Ltd. was then dissolved and thereafter the business was conducted by a corporation named “Daisy Chain, Inc.”. Tr. p. 21. No documentary evidence was introduced supporting this testimony, however.

"Duck" testified that he was president of "Chain, Ltd." and of "Chain, Inc.". Tr. pp. 23, 40. "Duck"’s argued that it was "Chain, Ltd.", not "Chain, Inc.", that made the sales for which the Department issued the Notice of Tax Liability, and that since the NPL was issued to him as a responsible officer of "Chain, Inc.", the wrong corporation, the assessment is defective.

The Department’s records show that the business was at all times operated under the registration number for "Chain, Inc.", which was 0000-0000, and sales tax returns were filed consistently reporting the sales incurred by the business under that name and number.

"Duck’s" argument fails for several reasons. First, the underlying sales and ROTA tax liability were reported to the Department under the IBT number issued by the Department to "Chain, Inc.", 0000-0000, and that is the number under which the NPL was issued. Finally, to prove its case, a taxpayer must present sufficient documentary evidence to support its claims for exemption. Testimony alone is not enough. Mel-Park Drugs, Inc. v. Department of Revenue, 218 Ill.App.3d 203 (1st Dist. 1991) There is no evidence of record, other than "Duck’s" testimony, that there were two corporations. Therefore, "Duck’s" assertion that the NPL was improperly addressed must fail.

The second issue in this case is whether "Duck" is a responsible person who willfully failed to file and pay retailers' occupation taxes for "Chain" as required by statute, and is, therefore, personally liable for the penalty imposed by section 13½ of the Retailers Occupation Tax Act ("Act") now that "Chain" is no longer in business and "Chain's" retailers' occupation taxes remain unpaid.

Once the Department introduced into evidence the NPL under the Director's certificate (Dept. Ex. No. 1), its *prima facie* case was made. Branson v. Dept. of Revenue, 168 Ill.2d 247 (1995) By operation of the statute, proof of the correctness of the penalty, including the willfulness element of the statute was established. *Id* at 260. At that point in the proceedings, "Duck" had the burden of proving that the penalty did not apply to him. *Id*. at 261. The record shows that he failed to do so.

Section 13 ½, in relevant part, provides as follows:

> (a) Any officer or employee of any taxpayer subject to the provisions of a tax Act administered by the Department who has the control, supervision or responsibility of filing returns and making payment of the amount of any trust tax imposed in accordance with that Act and who willfully fails to file the return or make the payment to the Department or willfully attempts in any other manner to evade or defeat the tax shall be personally liable for a penalty equal to the total

> amount of tax unpaid by the taxpayer including interest and penalties thereon. The Department shall determine a penalty due under this Section according to its best judgment and information, and that determination shall be *prima facie* correct and shall be *prima facie* evidence of a penalty due under this Section. Proof of that determination by the Department shall be made at any hearing before it or in any legal proceedings by reproduced copy or computer printout of the Department's record relating thereto in the name of the Department under the certificate of the Director of Revenue. Ill. Rev. Stat. 1991, ch. 120, ¶ 452½

Whether "Duck" is liable for the tax depends in the first instance on whether he is a responsible person under the statute. In applying the penalty tax, the Illinois courts look to federal cases involving § 6672 of the Internal Revenue Code[3] which contains language similar to the Illinois statute. Branson, *supra*. The fact that a person was an officer of a corporation does not, *per se*, mean that he was the person who had the duty to collect, account for and pay over the tax. Monday v. U.S., 421 F.2d 1210, (7th Cir. 1970), cert. den. 400 U.S. 821. However, the fact that another person may have had that responsibility does not mean that the officer was not also responsible. *Id*. The liability attaches to those who have the power and responsibility within the corporation for seeing that tax owed is paid and that responsibility is generally found in high corporate officials charged with general control over corporate business. *Id*. Responsibility is not a matter of knowledge, but rather a matter of status and authority. Mazo v. U.S., 591 F.2d 1151 (5th Cir. 1979)

In the instant case, "Duck" was president and 50% owner of "Chain" during the fall of 1990. He had check signing authority and he signed sales tax returns and checks to pay the tax liability shown on the returns. "Chain's" by-laws are not in evidence, so the record does not show what duties and responsibilities were vested in the president of the corporation.

However, the president of a corporation, is often the highest ranking officer in the corporation. As such, it is reasonable to conclude that by virtue of that office, the president is charged with the responsibility for management of the corporation and it is also reasonable to conclude that by such office, the president is responsible for all operations. Although, as "Duck" testified, "Chain" had several different individuals serving as general manager handling the day to day business of the corporation, as president, he had a duty to make sure the retailers' occupation taxes were paid as required. Therefore, "Duck's" position as president and 50% owner of "Chain" gave him the status and authority that made him a responsible person under the statute.

Finding that "Duck" was a responsible person, the next question is whether he willfully failed to pay over the retailers' occupation tax within the meaning of the statute. The concept of willfulness is not defined in the statute. The court in Monday, *supra*, noted that the concept, when used in criminal statutes, requires "bad

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[3] 26 U.S.C. § 6672.

purpose or the absence of justifiable excuse. *Id*. at 1215. The court then distinguished the meaning the term when used in civil actions by saying, "[R]ather, willful conduct denotes intentional, knowing and voluntary acts. It may also indicate a reckless disregard for obvious or known risks." *Id*; Dept. of Revenue v. Joseph Bublick & Sons, Inc., 68 Ill.2d 568 (1977).

The willfulness requirement "is satisfied if the responsible person acts with reckless disregard of a known risk that the trust funds may not be remitted to the Government. . .." Garsky v. U.S., 600 F.2d 86 (7th Cir. 1979) A high degree of recklessness is not required because if it were required, the purpose of the statute could be frustrated simply by delegating responsibilities within a business and adopting a "hear no evil -- see no evil" policy. Wright v. U.S., 809 F.2d 425 (7th Cir. 1987) A "responsible person is liable if he (1) clearly ought to have known that (2) there was a grave risk that withholding taxes were not being paid and if (3) he was in a position to find out for certain very easily." *Id*. at p. 427. Willfulness can be established by showing gross negligence as in a situation in which a responsible party ought to have known of a grave risk of nonpayment and who is in a position to easily find out, but does nothing. Branson, *supra*.

In this case, "Duck" was alerted to "Chain's" financial problems in the fall of 1990 when he began to get calls from creditors because they were not being paid. He signed sales tax returns and checks to pay the tax liabilities reflected on those returns. He testified that he did not receive regular reports from the accountants. "Duck" testified that in the fall of 1990 when he learned that "Chain" was having financial difficulties, he examined the books and records and spoke to the accountants and to the manager. He testified that he began getting verbal financial reports from management when he learned that "Chain" was failing. There is no testimony, however, that he ever asked the accountants or management what bills were being paid and what bills were not being paid.

The underlying sales tax liabilities in this case were incurred for the months of August 1990 through February 1991, a period of time during which "Duck" testified he was aware of "Chain's" financial problems. Since creditors were calling him to complain about not being paid, he should have known that there was a grave risk that liabilities to the Department were not being paid, yet there is nothing in the record indicating that he inquired into that possibility. Having had contact with the accountants who received "Chain's" bank statements and canceled checks from the bank, he easily could have inquired as to whether "Chain's" ROTA tax liabilities were being paid, but apparently he did not do this. These factors establish willfulness within the context of the statute and make him liable for the penalty assessed.

WHEREFORE, for the reasons stated above, it is my recommendation that the Department's Notice of Penalty Liability should be made final.

June 23, 1999 **ENTER:**

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Administrative Law Judge